


Annual Report 1996

NII Norsat International Inc.

Innovative Technology

Creative People

NII Norsat International Inc. is a technology company specializing in the design and manufacture of satellite and cable communications equipment for commercial applications, which it sells through its offices in Canada, the U.S., the U.K. and China, and through a global network of more than 35 distributors. Norsat also distributes consumer satellite equipment in Canada through its Aurora Distributing division and in the U.S. through its subsidiary, Diamond Pacific, Inc. Norsat has a proud history of achievement dating back to 1977 when it became the first Canadian company to design and install a personal satellite receiving system. It is this same pioneering spirit, reflected in the creative talents of its management and staff, its quality engineering and manufacturing, and its commitment to the development of innovative products, that continues to make Norsat a leader in the global satellite industry. NII Norsat International Inc. is a publicly traded company listed on the Toronto Stock Exchange (symbol NII) and NASDAQ (symbol NSATF).

Contents

On the cover: Adam Best, LNB Test Specialist; Tamara Thompson, Buyer; Dale Belsher, Vice President, Finance, CFO and Corporate Secretary; Don Filmer, Vice President, Engineering.

NORSAT

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Financial Summary

thousands of Canadian dollars	1996	1995*	1994*	1993*
Sales	**$ 57,494**	$ 48,773	$ 37,250	$ 18,649
Earnings before interest, taxes, depreciation and amortization	**2,738**	1,713	1,691	298
Net earnings (loss)	**2,069**	903	818	(361)
Cash generated by (used in) operations (before changes in non-cash operating working capital)	**3,005**	1,757	1,503	344

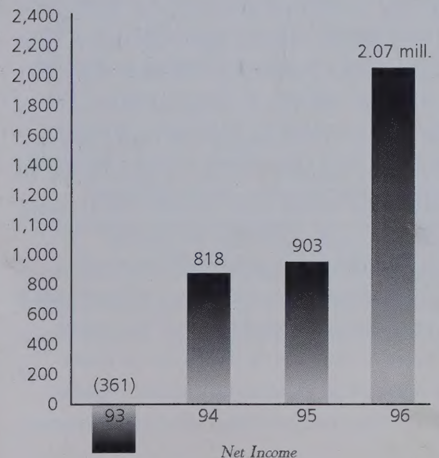
Financial position

thousands of Canadian dollars				
Total assets	**$ 30,596**	$ 27,333	$ 17,957	$ 13,359
Long-term debt (excluding current portion)	**81**	84	3,021	3,293
Shareholders' equity	**21,160**	20,161	9,948	6,147
Ratio of debt to equity	**0.45:1**	0.36:1	0.81:1	1.17:1

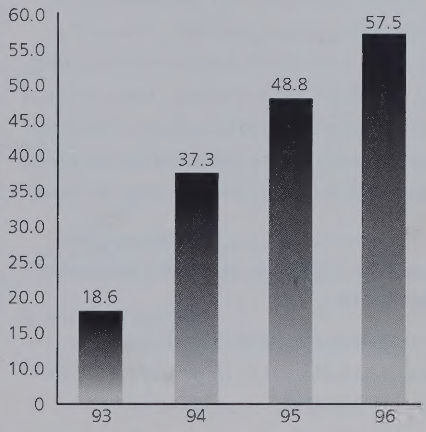
Per common share

Canadian dollars				
Net earnings (loss) – basic	**$ 0.11**	$ 0.05	$ 0.06	$ (0.05)
Cash generated by operations	**0.15**	0.10	0.11	0.04
Book value	**1.07**	1.02	0.66	0.61

**restated for prior period adjustment*



Net Income
in thousands of dollars



Annual Sales
in millions of dollars

Key Achievements

- *Achieved record financial results, increasing sales by 18 per cent to $57.5 million and more than doubling earnings to $2.07 million.*
- *Increased international sales of commercial products by 30 per cent and expanded our presence into new markets where demand for sophisticated communications technologies is accelerating.*
- *Initiated development of significant new products, including Ka-band low noise block downconverters (LNBs), key components for the development of a two-way, high-speed global communications infrastructure.*
- *Commenced shipments of N-Code II pay TV scrambling system components to China, establishing us as a leader in that market and creating a blueprint for profitable relationships in other developing countries where a combination of state-of-the-art technology and a unique marketing approach is required.*
- *Reorganized and expanded our U.S. consumer satellite distribution arm, Diamond Pacific, Inc., substantially increasing its margins and firmly establishing its profitability.*

Fiscal 1996 was a significant year for Norsat, marked by our increased development of innovative products for global markets and by our expanded international sales presence in new regions, where demand for sophisticated communications systems is accelerating rapidly. We also successfully met our annual financial targets and, in doing so, established new earnings and sales records. Net earnings for the year more than doubled, increasing by 129 per cent to $2.07 million or $0.11 per share, up from $903,457 or $0.05 per share in 1995. Sales increased by 18 per cent to $57.5 million, up from $48.8 million in 1995.

1996 also signalled a turning point for our organization both in terms of leadership and corporate focus. In October, I was pleased to assume the role of President and Chief Executive Officer and to take responsibility for leading Norsat and its dedicated team of management and staff into the 21st century.

Together with that change comes a renewed commitment to technological innovation and product development. Realization of Norsat's growth potential will depend to a significant extent on its ability to utilize its present strong financial position and the ongoing strong cash contributions from its North American consumer distribution operations to develop and acquire an expanded array of high-margin proprietary products and technologies.

This new focus is currently being implemented with a vigorous program to develop market-driven additions to our existing original equipment manufactured (OEM) product lines and with the dedication of additional engineering resources to the creation of a line of Ka-band low noise block downconverters (LNBs), to ensure our significant participation in that market as it develops. New product directions and potential acquisitions of new technologies are actively being pursued and initial opportunities identified are currently under evaluation.

Strong commercial sales support Norsat's technology focus

Our Commercial Products division, which focuses on international sales of LNBs and our OEM products, experienced another exceptional year, with sales increasing by 30 per cent and net profit virtually doubling over the previous year.

Sales of our Channel•On•Demand (COD) private video delivery system more than doubled in 1996. COD's increased international acceptance resulted from heightened marketing efforts, and was enhanced by our successfully obtaining ministerial approval for the product line in China and its inclusion in the U.S. government's purchasing database.

Asia Pacific represented a significant area of growth in 1996, with sales to the region up over 100 per cent, due principally to two contracts for our state-of-the-art N-Code II scrambling and descrambling technology finalized with Chinese customers. In tapping this vast market, we established a leadership position in the Chinese cable television industry, estimated to reach 93 million subscribers by the year 2000, and also created a blueprint for identifying opportunities and cementing sales in new regions that require sophisticated communications technologies.

Norsat's standing as the world's number one supplier of commercial LNBs remained intact in 1996 and we strengthened our industry-leading position by expanding into new markets. In Europe, sales of our commercial LNBs increased by 90 per cent, driven by the growth of the VSAT (Very Small Aperture Terminal) market, as corporate customers demanded more capacity and higher-end communications applications.

Strong sales of our commercial products enabled us to realize another significant achievement in 1996. Our manufacturing facility, which had experienced two years of consecutive losses due to under-utilization, operated at significantly higher capacity throughout the year and generated substantial returns.

The future belongs to satellite technology and Norsat

The satellite industry is poised for explosive growth, with worldwide revenues projected to increase from $9 billion in 1996 to $29 billion in 2000. This growth is being fuelled by the introduction of a host of new satellite services, aimed at bringing instant communications capabilities to millions worldwide.

No company is better positioned than Norsat to benefit from the satellite industry's projected growth. We have a strong balance sheet, limited debt, experienced management and a committed team of employees focused on developing new technologies and products.

We have also successfully demonstrated our ability to identify opportunities in emerging markets and to tailor our marketing approach to meet the demands of particular countries and cultures. This expertise, honed by our experience in China, will enable us to expand our presence in target regions like South America, Eastern Europe, India and Africa, where the use of satellite technology is expected to grow rapidly, as the ability to create an instant infrastructure is exploited to bring television, high-speed data and Internet access to users virtually overnight.

Our U.S. and Canadian consumer satellite distribution businesses provide us with distinct financial and marketing advantages. Both organizations have focused on building their leadership positions in their respective markets by offering a combination of superior consumer satellite equipment and services.

In 1996, Diamond Pacific, Inc., our U.S. operation, increased sales, expanded its branch network by two offices, diversified its product line and launched a high-profile marketing initiative to effectively differentiate itself from the competition. Aurora Distributing, our Canadian operation, increased sales by 18 per cent and capitalized on opportunities to sustain its growth by augmenting its current offerings with exciting new products like General Instrument's 4DTV system.

We are now utilizing Aurora and Diamond Pacific as a cost-effective means of delivering our own manufactured commercial products to customers across North America, generating additional sales opportunities.

This report, as you will read, not only provides a concise overview of the past year's operation, but also highlights the talents and creative efforts of our management and staff. It emphasizes the team effort involved in the four-year rebuilding process that has resulted in our current record sales and earnings performance.

The dedication of the 140-person Norsat team ensures that we will stay one step ahead in our rapidly evolving industry. I thank our team for its efforts and anxiously look forward to participating in the continued translation of our team's ideas and expertise into innovative Norsat technologies and communications solutions for growth markets worldwide.

Bruce H. Chapman
President & Chief Executive Officer

I also thank our shareholders for their continuing support and faith in our organization over the past year. I am confident that, with our renewed focus on technology, your confidence will be rewarded with strong performance, global expansion and continued significant achievement.

Bruce H. Chapman
President & Chief Executive Officer
April 15, 1997

Norsat's Commercial Products division recorded another very successful year. Overall, sales of our high-quality LNBs, COD and N-Code II systems, and our other OEM (original equipment manufactured) products increased by 30 per cent. Much of this growth was driven by sales into the Asia Pacific region, one of the world's fastest-growing markets in terms of the demand for satellite and cable communications technology, and by sales into Western Europe, which were fuelled by rapidly increasing demand for satellite-based, two-way communications systems.

Three members of Norsat's head office commercial sales team: Providing state-of-the-art technology, backed by a commitment to high-quality service. (from left: Catherine Marko, Teri Vincent and Sherri Binks.)

Norsat establishes a foothold in China

In 1996 Norsat finalized two major contracts for its N-Code II scrambling and descrambling technology. In July, Eastonk International Enterprises Corp. signed a Memorandum of Understanding for the purchase of key components for up to 3,000,000 N-Code II decoders to be built over the next five years. Three months later, Shenzhen Telecom Equipment Co. purchased components for an initial 100,000 N-Code II decoders, and estimated requiring components for another 2,000,000 units over the next few years.

In signing these contracts, Norsat has tapped a vast market for its N-Code II product, specifically designed for cable distribution networks, expected to be the only method of television signal dissemination which will be permitted in China. According to statistics provided by the Chinese Ministry of Film, Radio and Television, China expects to have approximately 93 million cable subscribers by the year 2000, with an annual growth rate of 7,000,000 per year.

Creating a blueprint for success in new regions

Norsat, through its experience in China, has also established a blueprint for identifying opportunities and forging profitable relationships in new markets. Our goal is to apply this experience in developing regions where the demand for communications technology is accelerating rapidly and the potential for sales of N-Code II and other Norsat OEM products is significant.

Sales of our Channel•On•Demand (COD) private video distribution system were much stronger in 1996. COD is now recognized as an industry standard and remains the product of choice for cruise ships, army bases and campuses. COD's acceptance was the result of substantially increased marketing efforts, which included a series of international trade show presentations to educate customers on the product's superior functionality and operational benefits. Acceptance was also facilitated by our obtaining product certification from the Chinese government and by our arranging its inclusion in the U.S. government's official purchasing database.

Norsat's standing as the world's number one supplier of commercial LNBs remained intact in 1996, with significant growth experienced in Europe, where sales of commercial LNBs increased by 90 per cent over the previous year.

Outlook

We expect increasing sales of our commercial products, particularly into the Asia Pacific area and Europe. We are also targeting new markets, like Russia and Eastern Europe, South America, India and Africa, where the demand for a satellite-delivered "instant infrastructure" is driving the need for state-of-the-art technology.

Three years ago, Norsat was virtually unknown in China. Today its name is synonymous with quality communications products for the cable television sector. In 1996, Norsat established itself as a leader in the Chinese cable television market by finalizing two major contracts for the sale of its N-Code II scrambling systems. *Led by our Vice President of Commercial Products, Wayne Meadows, the driving force behind our success in China has been the professional sales team of Douglas Chun, Louis Wu and Quiling Qin. This group's unique approach to finding "win-win" solutions with customers and sustaining the complex, often delicate relationships needed to thrive in China, has helped ensure Norsat's recognition as the provider of choice for pay television scrambling system requirements.*

Louis Wu
Manager, Sales & Business Development
Asia Pacific

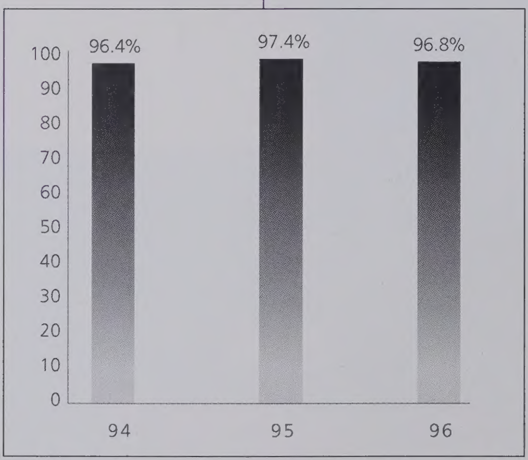
Douglas Chun
CATV Product Manager

Wayne Meadows
Vice President,
Commercial Products

Quiling Qin
Field Application Manager,
Beijing office

As sales of our OEM commercial products increased through 1996, our Surrey manufacturing facility operated at significantly higher volumes, enabling us for the first time to reduce the losses which resulted from its underutilization.

Our surface-mount facility principally produces the components for our modular Channel•On•Demand (COD) state-of-the-art delivery systems for private cable applications and the encoders and decoders for our N-Code II digital pay TV signal scrambling systems. Our in-house manufacturing capacity has enabled us to implement the stringent quality controls which ensure the reliability of these products.



Test first pass yield: Average for all product lines.

Strong commercial sales bolster manufacturing volumes

Our increased manufacturing volumes resulted from international marketing efforts for COD, as well as its certification by the Chinese Ministry of Film, Radio and Television. This recognition is significant given that approval must be received prior to the sale of any product to cable companies operating in China. We also achieved COD's inclusion in the U.S. government's purchasing database which itemizes products that may be purchased by federal agencies without requiring prior approval.

Increased manufacturing volumes were also supported by initial fulfilment of our delivery requirements for N-Code II system components under our Chinese sales contracts.

High-quality manufactured products our trademark

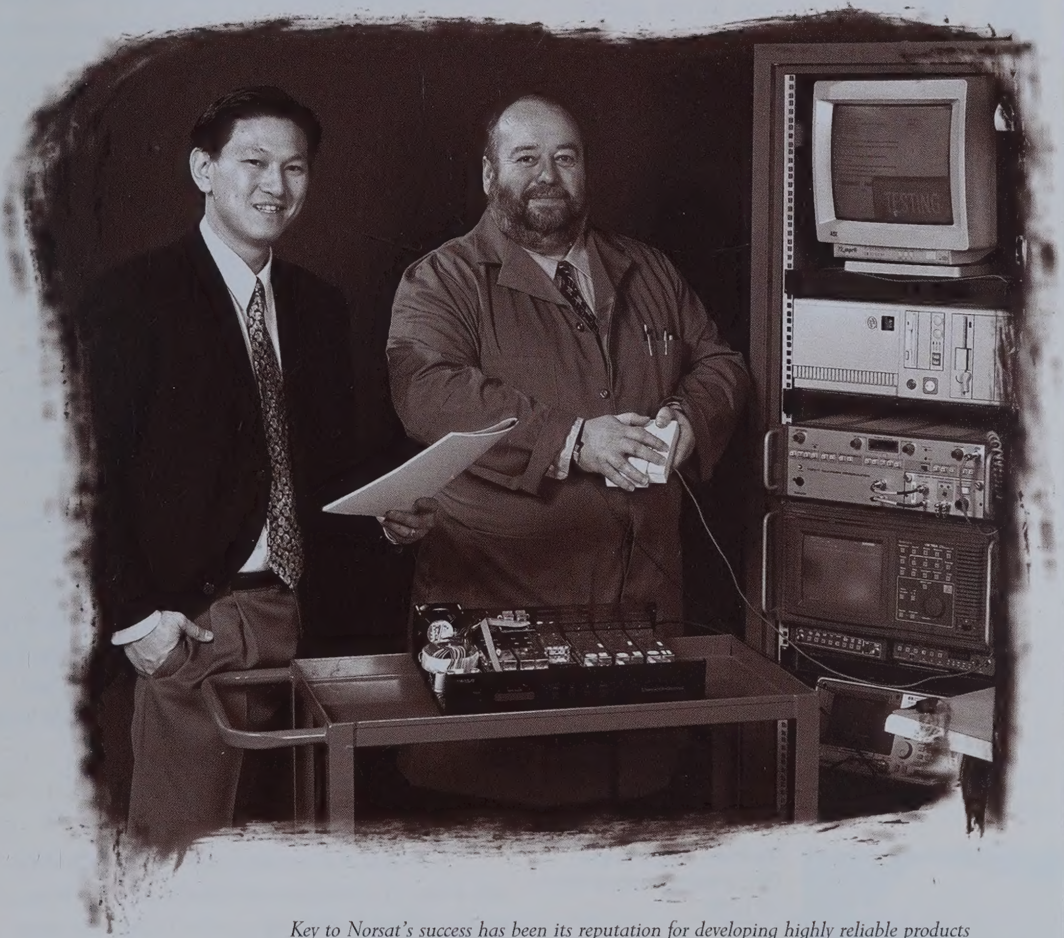
The in-field reliability of our commercial products is one of our principal competitive strengths. Our increased manufacturing volumes have not impacted the high-quality standards we have consistently met. Our first pass yield rate, the ability of a product to pass a stringent initial testing process, remained at an exceptionally high 97 per cent throughout the year.

Outlook

We are focused on ensuring that our manufacturing facility will continue to operate at increasing volumes. In addition to meeting enhanced demand for our existing technologies, we are dedicated to developing innovative, new products for in-house manufacture, such as our Ka-band consumer LNB, the initial production runs of which will be made in our own facility.

We are also arranging alliances with companies whose core products complement our manufacturing capabilities and, in the acquisition program we currently have underway, strong consideration is given to the extent to which increased usage of our manufacturing facilities would be realized.

To maintain our high-quality levels and increase our production capacity, an upgrade to our automated chip-shooter technology will be made in 1997.



Key to Norsat's success has been its reputation for developing highly reliable products recognized for superior performance. We consistently meet the ambitious standards of excellence we set. Our manufacturing team, anchored by Vice President Patrick Mann, focuses on establishing procedures to ensure that every product we manufacture meets the quality standards that have been our trademark for two decades. *Central to our quality initiatives is a sophisticated automated testing system which evaluates all of the cable headend products we manufacture. Powered by software designed in-house, this innovative solution – one of the many devised by our manufacturing team – has significantly reduced our testing costs and has enabled us to proudly maintain a 97 per cent first pass yield rate.*

Patrick Mann *Vice President, Manufacturing*	*Keith Andrew* *Manager, Manufacturing*

Norsat's success in the global market has been based on its ability to design and develop innovative products that target specific customer requirements, anticipate the evolving needs of a changing industry and focus on the unique technology demands of particular geographic regions. Norsat has established an enviable track record for designing and engineering "industry first" product prototypes and reliably following up with the introduction of commercially viable versions for worldwide markets.

Recognizing that product development remains key to our future, in 1996 we sharpened our focus on identifying and securing profitable new opportunities. In addition to augmenting current products to enhance their sales potential, we initiated development of new products that will place us at the centre of an exciting new satellite communications infrastructure.

In 1996, Norsat developed the world's first commercially viable Ka-band LNB.

Norsat engineers the next generation of LNB

Norsat is already recognized as the world's number one commercial supplier of low noise block downconverters (LNBs). Every satellite receiving system, regardless of its size or location, requires an LNB to function. LNBs sit at the focal point of a dish and convert incoming microwave signals into lower frequency electrical signals that can be easily and economically routed over standard coaxial cable to a remote receiver. Norsat currently sells more than 100 different types of LNBs, for various frequency bands and with various performance specifications.

Confirming our leadership role in the development of LNBs, in 1996 we commenced engineering work on the next generation of this product, which has resulted in our introduction of the world's first commercially viable Ka-band LNB. The Ka-band LNB is a significant achievement, as it enables us to place ourselves in the centre of an emerging global satellite communications framework.

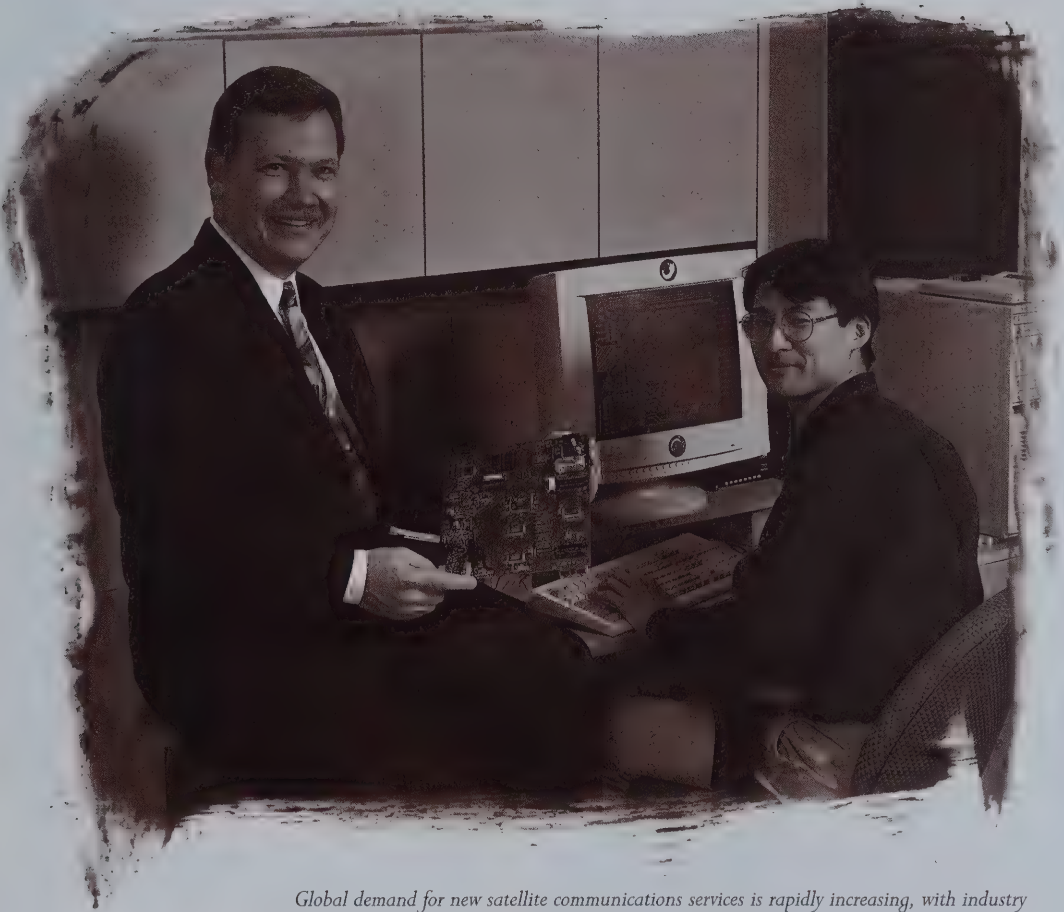
Large segments of the Ka-band spectrum, from 17 to 30 gigahertz, have been reserved for a wide range of high-speed, two-way digital communications services which address consumer demand for speedier access to the information superhighway. Companies such as Hughes (Galaxy/Spaceway), Microsoft/McCaw Cellular (Teledesic), AT&T (VoiceSpan) and GE Americom (Star System) are planning satellite-based communications services operating within the Ka-band broadcast spectrum.

In 1997, we plan to build up to 1,000 Ka-band field trial LNBs in our Surrey manufacturing facility. Given the growing global demand for two-way, high-speed communications services and the urgent need for the establishment of a cost-efficient "instant infrastructure" in developing countries, we expect sales of our Ka-band LNB to be a significant source of revenue over the next several years.

N-Code II enhancement supports marketability

N-Code II is Norsat's state-of-the-art addressable video scrambling system used in pay television systems. There are two parts to the N-Code II system: signal scrambling/encoding and descrambling/decoding. Norsat manufactures "headend" encoders that are installed in cable control facilities to scramble the pay channels and enable system operators to deliver pay services to their subscribers. We also design and provide the corresponding addressable decoding components required to descramble the signal at subscribers' residences.

Over the past two years, Norsat's product development team has worked diligently to finalize the commercial aspects of the N-Code II system and conduct extensive field trials with prospective customers in various parts of the world. As a result of these efforts, Norsat was successful in securing two contracts with cable TV providers in China. In 1997, our design team will continue to develop the N-Code II technology through integration and the addition of various levels of interactivity.



Global demand for new satellite communications services is rapidly increasing, with industry revenues expected to reach $29 billion by the year 2000. Ensuring that Norsat benefits from this phenomenal growth is a key responsibility of our product development and engineering team. Led by Vice President Don Filmer, this talented group specializes in identifying product opportunities and innovative directions for Norsat. Most recently, this team initiated the development and successful prototyping of the world's only commercially viable Ka-band low noise block downconverter – an important technological achievement given the significant role Ka-band systems are expected to play in the expansion of high-speed, two-way digital communications services. Norsat's product successes are the result of a visionary team focused on ensuring that we remain a leader in the development of innovative products for global markets.

Don Filmer
Vice President, Engineering

Wayne Takashiba
Engineering Project Manager

New QA series agile modulator developed

While selling N-Code II systems into China, Norsat's product development team identified a customer need and translated it into a product development opportunity. The result was our QA series agile modulator.

The QA operates like our Channel•On•Demand (COD) system, collecting video and audio signals and converting them into television channel frequencies suitable for distribution along a coaxial cable to a number of cable subscribers. However, unlike the COD system which is targeted to smaller private networks, the QA provides higher output power to accommodate a larger number of end-users, such as those located within a citywide cable network.

Norsat's QA series agile modulator: A graphic illustration of Norsat's unique ability to identify a market need and develop a product with a ready customer base.

Norsat anticipates a large market for sales of its QA series modulator, particularly in China where the cable TV infrastructure is quickly emerging. Our success in designing the QA underscores the unique ability of our engineers to research a region, identify product opportunities and design a product to suit a guaranteed customer base.

1996: The year of Channel•On•Demand

1996 was the year that our Channel•On•Demand (COD) video delivery system for private cable applications became acknowledged as an industry-leading product. We strengthened COD's marketability considerably in 1996 by adding a universal output selector, enabling it to operate in all regions of the world without requiring any special design or manufacturing adjustments. Expansion of the COD product line is underway, aimed at providing specialized features that will further support its marketability and application within small cable networks.

Our strength: Identifying new opportunities

We continue to identify new opportunities to apply our expertise in developing innovative products for exciting new markets. In 1996, Norsat, through the Canada West Telecom Group, played a key role in developing a satellite-based distance learning project. As part of this group, which is seeking to market turn-key distance learning solutions, Norsat will provide a wide range of necessary hardware, including LNBs, satellite receivers and antennas. The project has received a considerable amount of interest from international financial and educational institutions, and is currently before several motivated buyers.

Outlook

In addition to the continuing customer-driven enhancements which our engineering team is making to our COD and N-Code II product lines, work is underway to expand our QA series modulator to include much of the functionality of our full COD system. This will provide us with a lower priced alternative for cable system operators in emerging markets where affordability is key.

Work is also well underway on our second generation of Ka-band LNB prototypes, with the expectation that initial production of field trial units of a consumer version will commence this year.

Our product development team is also exploring opportunities to supply specialized products and microwave communications equipment to companies planning to establish Local Multipoint Communications Systems (LMCS) in Canada. Despite the somewhat chaotic state of the industry, we remain in discussion with key players, confident that our equipment will play a role in the establishment of this proposed new information infrastructure.

Norsat's U.S. distribution arm Diamond Pacific, Inc. (DPI), was both reorganized and expanded in 1996. Under the leadership of President Ed Johnson, who joined the organization during the second quarter, several key initiatives were launched to increase sales and margins, and establish DPI as the premium provider of consumer satellite equipment and services in the U.S.

To enhance the appeal of its offering and support its centrepiece Hughes system, DPI has expanded and diversified its product line to include high-profile, consumer-friendly products, such as the Toshiba, Hitachi and Panasonic Digital Satellite System (DSS) offerings, as well as Sherwood's line of home theatre electronics products. DPI has also added the popular Silent Witness line of surveillance equipment, to create cross-selling synergies not only for consumer satellite and home theatre products, but also for Norsat's proprietary commercial equipment that can be used to distribute the surveillance signals.

The "Diamond Advantage" quality program supports DPI's industry-leading position

Perhaps the most significant strategy initiated by DPI was the launch of its "Diamond Advantage" quality marketing program, used in all promotional materials. In addition to establishing DPI as a provider of premium products and services, this vision has heightened the organization's profile in the competitive U.S. market, which is expected to reach 16 million subscribers by the year 2002. It has also effectively differentiated DPI from its competition and has assisted it in concluding important distribution agreements with major equipment manufacturers.

To support its continued strong growth and enhance sales opportunities throughout the Western U.S., DPI extended its distribution network to eight offices in 1996 by opening new branches in Denver and Las Vegas.

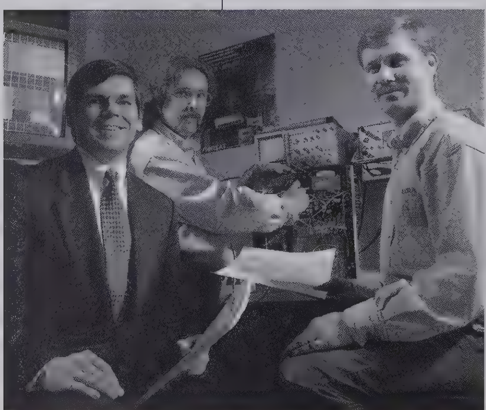
Outlook

The outlook for DPI continues to be extremely positive. The Company plans to open another three branches in 1997 and is focused on expanding its distribution network by attracting additional dealers through the continued provision of a wide range of quality products and services, including a competitive consumer finance program. DPI is also focused on identifying corporate synergies with Norsat, particularly by supporting the growth of its Commercial Products division by cost-efficiently distributing its proprietary products to U.S. customers seeking high-technology solutions delivered by a local supplier.

Diamond Pacific's Consumer Finance team, pictured here with President Ed Johnson, plays an integral part in supporting DPI's industry-leading position, solidified in 1996 through the "Diamond Advantage" marketing program. (from left: Brenda MacLean, Sarah McAleese, Ed Johnson and Gabriela Guisado.)

Our Canadian consumer satellite equipment division, Aurora Distributing, experienced steady growth in 1996, reporting an 18 per cent increase in sales. With nine offices across Canada, Aurora remains the country's largest and most successful satellite equipment distributor, offering a wide range of premium products and specialized services.

Under the direction of Norsat Vice President and Aurora General Manager Lindsay Ryerson, the division has adopted several strategies to maintain its leadership position in the increasingly competitive domestic marketplace.



As Canada's largest and most successful consumer satellite equipment supplier, Aurora's commitment to service and quality extends through all levels of the organization, from purchasing, sales and marketing, to shipping and service. General Manager of Aurora Distributing, Lindsay Ryerson sits in during the Service department's evaluation of one of Aurora's quality products. (from left: Lindsay Ryerson, Bruce Clayton and Carl Jaehrlich.)

Strengthening our competitive position with exciting new products

One of these strategies is the continuous addition of new product lines to meet dealer expectations and preferences. Aurora recently added General Instrument's new 4DTV system as a core product. This system represents a revolutionary dimension in satellite-delivered entertainment, as it is capable of capturing both the analogue and the digital programming offered by C-band (large dish) and Ku-band (small dish) services.

Aurora, in conjunction with General Instrument, recently held a series of educational seminars across Canada to introduce the 4DTV product to dealers and highlight its many exciting advantages and features. Given its adoption by one of Canada's first Direct-To-Home (DTH) satellite providers and its appeal to existing C-band customers, 4DTV is expected to be a significant product in Aurora's future.

In addition to fortifying its offering with new core products, Aurora is supporting its national growth by expanding its distribution channels, diversifying its offerings with complementary products like home theatre electronics equipment and new accessories, and heightening its promotional activities to emphasize that it is not only the largest, but also the most trusted and knowledgeable distributor in Canada.

Outlook

Aurora expects to continue in its position as the largest consumer satellite equipment distributor in Canada. Continued growth in 1997 will be fuelled by expanding product lines, increasing the number of marketing channels used, and providing additional promotion and support across all product lines.

Financial Information

RESULTS OF OPERATIONS

Norsat reported record sales and earnings in 1996, with an increase in net earnings more than double that of 1995. Net earnings increased by 129% to $2,069,490 or $0.11 per share, up from $903,457 or $0.05 per share in 1995.

Sales for the year ended December 31, 1996 increased 18% to $57,493,621, up from $48,773,383 during the previous year. Gross margin also increased to $12,646,295 or 22% of sales, versus $9,826,548 or 20% of sales in 1995.

Earnings before interest, taxes, depreciation and amortization for 1996 increased to $2,738,235, compared to $1,713,250 in 1995.

These results indicate Norsat's strong position in the global satellite market and reflect the momentum of the prior year being carried forward into 1996. In particular, the Commercial Products division, which focuses on worldwide sales of high-margin satellite and cable communications equipment, increased international sales of low noise block downconverters (LNBs) and our original equipment manufactured (OEM) products by 30 per cent and virtually doubled its net profit over the previous year.

The principal factor in the growth of the Commercial Products division during the year was Norsat's ability to maintain its standing as the world's number one supplier of commercial LNBs. This industry-leading position was strengthened by our expansion into new markets. In Europe, in particular, sales of our commercial LNBs increased by 90 per cent, driven by rapid growth in the VSAT (Very Small Aperture Terminal) market.

Additionally, sales of our OEM products enabled our manufacturing facility, which had experienced two consecutive years of losses due to underutilization, to operate at significantly higher capacity throughout the year.

Asia Pacific was another significant area of growth in 1996, due principally to two contracts with Chinese cable system suppliers for our state-of-the-art N-Code II pay TV scrambling and descrambling technology. The first shipments under these contracts were made in 1996 and will continue through 1997.

Norsat's U.S. distribution subsidiary, Diamond Pacific, Inc. (DPI), completed its reorganization, increased its gross margins and established the formula for profitability in 1996. Strategic marketing initiatives which were launched during the year to establish DPI as a provider of premium products and services have heightened the organization's profile in the competitive U.S. market. These initiatives have also effectively differentiated DPI from its competition and have assisted it in concluding distribution agreements with major equipment manufacturers.

Norsat's Canadian consumer satellite equipment division, Aurora Distributing, experienced steady growth in sales in 1996, reporting an 18% increase over the previous year. Aurora remains the country's largest and most successful satellite equipment distributor. Like DPI, Aurora has established itself as the provider of premium products and services which differentiates it from the competition.

Operating expenses increased to $10,775,159 in 1996, compared to $8,921,271 in 1995. As Norsat continued its growth in 1996, operating expenses were maintained at approximately the same percentage of sales (18.5%) as in the previous year.

The components of these expenses were:

- Selling, general and administrative expenses increased to $9,564,691, compared to $7,766,108 in 1995. This was due not only to an increase in selling costs proportionate to our increase in sales, but also reflected an increase in selling costs due to our restructuring of sales incentive compensation, particularly in the Commercial Products division where reinforcement of sales of our higher-margin products was required. In 1996 Norsat also made a commitment to increase its investor communications efforts, and personnel and associated expenses increased accordingly. Additionally, directors and officers liability insurance was added to administrative expenses this year. Finally, increases in certain administrative expenses occurred in the year due to the overall growth in our business, however, tight policies to control purchasing and expenses are being maintained.
- Amortization of capital assets and goodwill increased to $867,099 in 1996, from $807,973 in the previous year. The increase in amortization expense resulted from capital asset expenditures of $572,171 during the year, primarily for new test equipment and facilities for our manufacturing and product development departments, as well as for computer equipment required to accommodate the growth of our Commercial Products division.
- Product development and engineering costs were $343,369 virtually unchanged from $347,190 in 1995. In spite of the reduced amount expended on product development in the past two years, Norsat has focused its attention on products aimed at specific market segments and customer requirements. As a result, we have established a track record for designing and engineering high-quality "industry first" products for worldwide markets.

Bank charges and interest on short-term debt for 1996 were $344,115, virtually unchanged from $345,322 in 1995. The growth in net earnings in the 1996 fiscal year allowed Norsat to finance internally the growth in accounts receivable and inventory that occurred due to increased sales. As a result, utilization of our bank line of credit was maintained at the same levels as 1995 and the resulting interest expense was similar to that incurred in 1995. Interest on long-term debt for 1996 was $105,574, down from $196,551 in 1995, as a result of the repayment of our term loan with Mutual Life of Canada on August 31, 1996, which eliminated the interest being paid thereon.

Other income was $648,043 in 1996, compared to $540,053 in 1995, and represents revenue generated from prudent investment of our cash resources, which is planned to be employed to fund future business opportunities consistent with our growth plans.

Net earnings for the year were $2,069,490, with basic earnings per share of $0.11, which is more than double the results in 1995 where net earnings were $903,457 and basic earnings were $0.05 per share. These results reflect Norsat's ability to utilize its strength and position in the satellite industry to capitalize on the growth in its target markets.

LIQUIDITY AND CAPITAL RESOURCES

Working capital increased to $15,651,405 in 1996, up from a positive position of $14,406,099 in 1995. The strong working capital position and the virtual elimination of long-term debt provides Norsat with a very solid balance sheet to capitalize on new opportunities.

Cash generated by operations before financing working capital was $3,004,570 in 1996, up from $1,757,175 in 1995.

In August 1996, the Company utilized funds generated from operations to pay out its term loan due to Mutual Life of Canada in the amount of $450,000.

From June 18, 1996 to December 17, 1996, the Company acquired 481,900 of its own shares pursuant to a normal course issuer bid for cash consideration of $1,112,840.

During 1996 the Company received $19,657 through the exercise of options to purchase 17,005 of its common shares. The Company currently reports 19,753,410 common shares as issued.

The Company has a $4,000,000 operating line of credit in the form of overdrafts and letters of credit. The security for these credit facilities consists of a first security interest in all of the Company's personal property and assignments of its insurance and inventory. These credit facilities bear interest at the rate of 1% of amounts guaranteed and at the rate of prime plus 1% for operating loans.

The Company's U.S. subsidiary, Diamond Pacific, Inc. has a US $1,000,000 revolving line of credit which is secured by the Company through a U.S. $1,000,000 standby letter of credit. The line of credit bears interest at the reference rate publicly announced from time to time by Diamond Pacific's bank.

A claim has been made against the Company and certain other parties totalling $55 million plus interest and legal costs for damages alleged to have resulted from the distribution and sale of digital satellite receiving/decoding systems in Canada, in alleged contravention of certain statutory provisions and rights, certain contractual rights and certain copyrights. The areas of law involved in this claim are complex and relatively unexplored, and the outcome thereof is uncertain. The Company is vigorously defending this claim and does not believe it has any obligation in respect thereof.

Management believes that Norsat is well positioned to capture the opportunities that present themselves in the global satellite industry. Norsat's strong working capital position provides excellent liquidity for realization of new business opportunities and for provision of the funding required to sustain growth in its Commercial Products division, its U.S. distribution subsidiary and its Canadian consumer satellite equipment division.

The consolidated financial statements have been prepared by management, which is responsible for the integrity and objectivity of this information. These statements have been prepared in conformity with generally accepted accounting principles and, where appropriate, include some amounts that are based on management's best estimates and judgements. The financial information presented elsewhere in this annual report is consistent with that in the consolidated financial statements.

A system of internal accounting and administrative controls is maintained by management in order to provide reasonable assurance that transactions are appropriately authorized, assets are safeguarded and financial records properly maintained to provide accurate and reliable financial statements.

The Board of Directors, through its Audit Committee, oversees management's responsibilities for financial reporting and internal control. The Audit Committee meets with management and the independent auditors to discuss auditing and financial matters and to review the consolidated financial statements and the independent auditors' report. The Audit Committee reports its findings to the Board for consideration in approving the financial statements for issuance to the shareholders.

The consolidated financial statements have been audited by KPMG, Chartered Accountants, who were appointed by the shareholders. The auditors' report outlines the scope of their examination and their opinion on the consolidated financial statements.

Bruce H. Chapman
President and Chief Executive Officer

Dale B. Belsher
Vice President, Finance and
Chief Financial Officer

We have audited the consolidated balance sheets of NII Norsat International Inc. as at December 31, 1996 and 1995 and the consolidated statements of earnings, retained earnings (deficit) and changes in financial position for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1996 and 1995 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles. As required by the British Columbia Company Act, we report that, in our opinion, these principles have been applied on a consistent basis.

KPMG

Chartered Accountants

Surrey, Canada
March 7, 1997

Consolidated Balance Sheets

NII Norsat International Inc.

As at December 31,	**1996**	1995 *Restated (note 16)*
Assets		
Current assets:		
Cash and cash equivalents	**$ 8,775,167**	$ 5,959,284
Marketable securities	**—**	2,397,963
Accounts receivable (note 2)	**6,341,508**	6,100,555
Inventory (note 3)	**9,712,828**	6,757,369
Prepaid expenses	**176,087**	278,985
	25,005,590	21,494,156
Investment (note 4)	**982,200**	982,200
Capital assets (note 5)	**2,423,511**	2,415,415
Deferred costs, net of accumulated amortization	**134,328**	118,595
Goodwill, net of accumulated amortization of $706,924 (1995 – $403,900)	**2,049,962**	2,322,984
	$ 30,595,591	$ 27,333,350
Liabilities and Shareholders' Equity		
Current liabilities:		
Bank indebtedness (note 6)	**$ 3,850,115**	$ 2,752,450
Accounts payable and accrued liabilities (note 7)	**5,500,962**	3,782,321
Current portion of long-term debt (note 8)	**3,108**	553,286
	9,354,185	7,088,057
Long-term debt (note 8)	**81,070**	84,178
Shareholders' equity:		
Share capital (note 9)	**19,537,882**	26,812,441
Retained earnings (deficit)	**1,599,540**	(6,651,326)
Cumulative translation adjustment	**22,914**	—
	21,160,336	20,161,115
	$ 30,595,591	$ 27,333,350

Commitments (note 13)
Prior period adjustment (note 16)
Contingency (note 17)

See accompanying notes to consolidated financial statements.

On behalf of the Board:

Director

Director

Consolidated Statements Of Earnings

NII Norsat International Inc.

Years ended December 31,	**1996**	**1995** *Restated (note 16)*
Sales	**$ 57,493,621**	$ 48,773,383
Cost of sales	**44,847,326**	38,946,835
	12,646,295	9,826,548
Expenses:		
Selling, general and administrative	**9,564,691**	7,766,108
Amortization of capital assets and goodwill	**867,099**	807,973
Product development	**343,369**	347,190
	10,775,159	8,921,271
Earnings before interest costs and other items	**1,871,136**	905,277
Bank charges and interest on short-term debt	**(344,115)**	(345,322)
Interest and financing costs on long-term debt	**(105,574)**	(196,551)
Other income	**648,043**	540,053
	198,354	(1,820)
Net earnings	**$ 2,069,490**	$ 903,457
Net earnings per share:		
Basic	**$ 0.11**	$ 0.05
Fully diluted	**$ 0.11**	$ 0.05

See accompanying notes to consolidated financial statements.

Consolidated Statements Of Retained Earnings (Deficit)

NII Norsat International Inc.

Years ended December 31,	**1996**	1995 *Restated (note 16)*
Deficit, beginning of year, as previously reported	**$ (6,681,376)**	$ (7,084,833)
Prior period adjustment (note 16)	**(469,950)**	(469,950)
Deficit, beginning of year, restated	**(6,651,326)**	(7,554,783)
Elimination of deficit prior to restatement (note 9(g))	**6,181,376**	—
Net earnings	**2,069,490**	903,457
Retained earnings (deficit), end of year	**$ 1,599,540**	$ (6,651,326)

See accompanying notes to consolidated financial statements.

Consolidated Statements Of Changes In Financial Position

NII Norsat International Inc.

Years ended December 31,	**1996**	1995 *Restated (note 16)*
Cash provided by (used for):		
Operations:		
Net earnings	**$ 2,069,490**	$ 903,457
Items not involving cash:		
Amortization of capital assets and goodwill	**867,099**	807,973
Amortization of deferred costs	**67,981**	45,745
Changes in non-cash operating working capital	**1,023,090**	(1,596,130)
Cash generated by operations	**4,027,660**	161,045
Financing:		
Issue of special warrants	**—**	5,022,355
Issue of common shares	**19,657**	4,287,372
Repurchase common shares	**(1,112,840)**	—
Principal payments on long-term debt	**(553,286)**	(951,608)
Conversion of debt to shares	—	(1,822,340)
	(1,646,469)	6,535,779
Investments:		
Purchase of capital assets	**(572,171)**	(558,292)
Decrease (increase) in deferred costs	**(83,714)**	96,309
Increase in goodwill	**(30,002)**	—
Purchase of investment	**—**	(982,200)
Acquisitions of businesses	**—**	(1,654,635)
	(685,887)	(3,098,818)
Cumulative translation adjustment	**22,914**	—
Increase in cash position	**1,718,218**	3,598,006
Cash position, beginning of year	**3,206,834**	(391,172)
Cash position, end of year	**$ 4,925,052**	$ 3,206,834

Cash position is defined as cash and cash equivalents less bank indebtedness

See accompanying notes to consolidated financial statements.

Years ended December 31, 1996 and 1995

The Company was incorporated October 15, 1982 under the laws of the Province of British Columbia and commenced operations November 1, 1982. The Company operates in the satellite communication industry.

1. Significant accounting policies:

(a) Principles of consolidation:

The consolidated financial statements are prepared in accordance with generally accepted accounting principles in Canada and include the accounts of the Company and all subsidiaries. All subsidiaries are wholly-owned.

(b) Cash and cash equivalents:

Securities with original maturities of three months or less when purchased are considered to be cash equivalents.

(c) Inventory:

Inventories of distribution products are stated at the lower of weighted average cost and net realizable value. Inventories of manufactured finished products and work in progress are stated at the lower of cost and net realizable value. Parts and supplies inventory is stated at the lower of cost and replacement cost.

(d) Capital assets:

Capital assets are stated at cost. Amortization is provided using the following methods and annual rates which approximate the useful life of the assets:

Asset	Basis	Rate
Equipment	Straight-line	10-20%
Furniture and fixtures	Straight-line	10%

Leasehold improvements are amortized over the shorter of the term of the lease or their estimated useful life.

(e) Investment:

The investment in Cyberion Networking Corp. is accounted for using the equity method.

(f) Deferred costs:

Pre-operating branch start-up costs are amortized on a straight-line basis over a three year period from the date the branch commences operations.

(g) Goodwill:

Goodwill is amortized on a straight-line basis over an eight to ten year period.

(h) Foreign currency translation:

The Company translates its integrated foreign operation using rates of exchange prevailing at the balance sheet dates for monetary items, historic exchange rates for non-monetary items (including depreciation) and average rates of exchange during the year for revenues and expenses.

The resulting gains or losses are charged to income except for those relating to monetary items having a fixed life greater than one year, which are deferred and amortized over the life of the monetary item.

The Company translates its self-sustaining foreign operations using rates of exchange at the balance sheet dates for assets and liabilities and at average rates of exchange during the year for revenues and expenses.

The resulting gains and losses are shown separately in the shareholder's equity section of the balance sheet.

During the year the Company considered its US foreign operation to have become self-sustaining.

1. Significant accounting policies (continued)

(i) Earnings per share:

Basic earnings have been calculated based on the weighted average number of shares outstanding (net of shares held in treasury) during the year. Fully diluted earnings per share have been calculated based on basic earnings per share adjusted for the effect of the potential exercising of options.

(j) Financial instruments:

The Company has applied the accounting standard with respect to the presentation of financial instruments on a retroactive basis. Additional note disclosure has been added but no other changes were required.

(k) Use of estimates:

The presentation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas requiring the use of management estimates relate to the determination of net recoverable value of assets, useful lives for depreciation, amortization and provisions for contingencies.

2. Accounts receivable:

As at December 31,	**1996**	**1995**
Trade	$ 5,555,529	$ 5,455,612
Other	785,979	644,943
	$ 6,341,508	$ 6,100,555

Accounts receivable other includes interest free loans, totalling $416,000 (1995 - $50,000) due from an officer and former officer of the Company. The amounts due are payable upon the sale of certain shares of the Company held by the borrowers.

3. Inventory:

As at December 31,	**1996**	**1995**
Distribution products	$ 8,232,328	$ 5,554,259
Work in progress	259,395	102,289
Parts and supplies	1,221,105	1,100,821
	$ 9,712,828	$ 6,757,369

4. Investment:

As at December 31,	**1996**	**1995**
Cyberion Networking Corp.	$ 982,200	$ 982,200

On May 1, 1995, the Company incorporated Direct PC Internet Corp. ("Direct PC"), as a wholly-owned subsidiary of the Company, to operate as an internet service provider. On June 30, 1995, the Company acquired 65% of the share capital of Cyberion Net-working Corp. (formerly Shogun Properties Corp.) ("Cyberion") for $355,770. Cyberion did not have an active business. On July 31, 1995, Cyberion acquired 100% of the assets of Direct PC, which had net assets of $322,521 at that date. Cyberion in 1995 and 1996 issued additional shares pursuant to underwriting agreements in which the Company did not participate. At December 31, 1996, the Company owned 24% (1995 - 30%) of Cyberion. Equity losses, related to the investment, have been offset by gains on dilution of the Company's ownership percentage.

5. Capital assets:

As at December 31, 1996		Cost		Accumulated amortization		Net book value
Equipment	$	3,465,498	$	1,839,686	$	1,625,812
Furniture and fixtures		714,308		396,317		317,991
Leasehold improvements		764,795		468,778		296,017
Product development equipment		1,141,348		1,078,148		63,200
Leased equipment		338,305		217,814		120,491
	$	6,424,254	$	4,000,743	$	2,423,511

As at December 31, 1995		Cost		Accumulated amortization		Net book value
Equipment	$	3,116,086	$	1,482,089	$	1,633,997
Furniture and fixtures		601,928		354,130		247,798
Leasehold improvements		697,882		392,550		305,332
Product development equipment		1,118,124		1,042,952		75,172
Leased equipment		338,305		185,189		153,116
	$	5,872,325	$	3,456,910	$	2,415,415

6. Bank indebtedness:

The Company's operating line of credit is available in the form of overdrafts and letters of credit. The security for the credit facilities consists of a first security interest in all of the Company's personal property, subject only to the interests of the term loan (note 8), assignment of insurance and inventory. These credit facilities bear interest at rates ranging from 1% on guarantees to prime plus 1% for operating loans.

During the year, the Company's subsidiary, Diamond Pacific Inc. ("DPI") entered into a revolving line of credit with a major bank for U.S. $1,000,000. This line of credit is secured by the Company through a U.S. $1,000,000 standby letter of credit. The line of credit bears interest at the bank's reference rate, as publicly announced from time to time.

7. Accounts payable and accrued liabilities:

On June 15, 1995, DPI entered into an agreement with a financial institution to provide advances to fund acquisition of inventory or other working capital requirements of up to $2,728,000 (U.S. $2,000,000). These outstanding amounts do not bear interest during the normal payment period, with interest accruing thereafter at 1.5 to 1.75% per month. At December 31, 1996 no amount was outstanding under this facility. At December 31, 1995 $356,274 was outstanding under this facility and is included in accounts payable. The arrangement is secured by a $1,364,000 (U.S. $1,000,000) letter of guarantee from the Company and a first charge on the assets of DPI, including inventory, equipment and accounts receivable. This arrangement was replaced during the year by a revolving line of credit referred to in note 6.

8. Long-term debt:

As at December 31,		1996		1995
Mutual Life of Canada term loan payable, with interest at 12.47% repayable in monthly instalments of $12,500 until August, 1996 at which time the remaining balance is due. The term loan is secured by a first charge on tangible (excluding accounts receivable and inventory) and intangible assets and a second charge on accounts receivable and inventory of the Company	$	—	$	550,000
0% Subordinated debentures, due on June 30, 1998		76,000		76,000
Long-term obligations under capital leases		8,178		11,464
		84,178		637,464
Current portion of long-term debt		3,108		553,286
	$	81,070	$	84,178

Principal payments on long-term debt required for fiscal years subsequent to December 31, 1996 are as follows:

1997	$	3,108
1998		81,070

9. Share capital:

The Company is authorized to issue 50,000,000 common shares without par value.

Common shares issued and fully paid:

	Number of Shares		Amount
Balance at December 31, 1994	15,021,555	$	17,502,714
Upon exercise of underwriter's warrants	50,000		107,500
Upon consideration paid for acquisition (note 10)	1,397,250		1,723,836
Upon conversion of bonds into common shares	1,300,000		1,596,591
Upon exercise of special warrants	1,300,000		5,022,355
Upon exercise of stock options	667,600		859,445
Balance at December 31, 1995	19,736,405	$	26,812,441
Elimination of deficit by paid-up capital reduction (note 9(g))	—		(6,181,376)
Upon exercise of options	17,005		19,657
	19,753,410	$	20,650,722
Shares purchased during the year and not cancelled (note 9(i))			(1,112,840)
Balance at December 31, 1996	19,753,410	$	19,537,882

(a) During the year ended December 31, 1995, the Company issued 50,000 common shares upon exercise of underwriter's warrants.

(b) On January 1, 1995, the Company issued 1,397,250 common shares at $1.60 per share (for total value of US $1,620,000) and received $1,723,836 net of issue expenses as consideration for the acquisition of all the issued share capital of Rexcom Inc. and Durex Satellite Inc. described in note 10).

(c) On June 15, 1995, the Company issued 1,300,000 common shares on conversion of U.S. $1,300,000 bonds on the basis of 1 common share for each U.S. $1.

(d) On July 17, 1995 the Company issued through a private placement 1,300,000 special warrants at a price of $4.20 per warrant and received $5,022,355 net of issue expenses. Each warrant was exchanged into one common share of the Company during 1995.

(e) During the year ended December 31, 1995, the Company issued 667,600 common shares upon exercise of stock options granted.

(f) During the year ended December 31, 1995, the Company granted to certain of its directors, officers and employees options entitling them to purchase up to 590,000 common shares of the Company. The options are exercisable at prices between $4.45 and $4.90 per share on or before expiration dates September 5, 2000 and September 20, 2000.

(g) At the Company's annual general meeting on May 29, 1996, the shareholders approved a $6,181,376 reduction in the share capital of the Company, with the corresponding elimination of the deficit of $6,181,376 at December 31, 1995 (prior to restatement).

(h) During the year ended December 31, 1996, the Company issued 17,005 common shares upon exercise of stock options granted.

(i) From June 18, 1996 to December 17, 1996, the Company acquired 481,900 of its own shares pursuant to a normal course issuer bid for cash consideration of $1,112,840. The purchase price exceeded the Company's average issue price by $458,260 which will be charged to retained earnings when the shares are cancelled. At December 31, 1996 these shares were not cancelled by the Company.

(j) During the year ended December 31, 1996, the Company granted to certain of its officers and employees options entitling them to purchase up to 550,000 common shares of the Company. The options are exercisable at prices between $2.00 and $3.10 per share on or before various expiration dates ranging from January 23, 2001 to October 25, 2002.

(k) At December 31, 1996, 1,423,295 (1995 - 930,300) stock options were outstanding. During the year 40,000 stock options expired without being exercised.

10. Acquisitions:

Effective January 1, 1995, the Company acquired Rexcom Inc. ("Rexcom") and Durex Satellite Inc. ("Durex") who collectively trade as "Durite Antenna Supply Company", by exchanging 1,397,250 common shares of the Company fair valued at $1,723,837 (U.S. $1,259,000), net of issue expenses, for all of the issued and outstanding share capital of Rexcom and Durex. The fair value of the shares is derived from their quoted market value at the date of acquisition less adjustment to reflect quantities traded and price fluctuations.

Assets and liabilities acquired were as follows:

Assets acquired:		
Cash	$	249,179
Accounts receivable		209,621
Inventory		685,988
Prepaid expenses		22,033
Capital assets		13,703
Goodwill		978,940
		2,159,464
Liabilities assumed:		
Accounts payable		(435,628)
Net assets acquired	$	1,723,836
Consideration given:		
Issue of common shares	$	1,723,836

11. Income taxes:

At December 31, 1996, the Company has a $1,230,000 (1995 - $3,500,000) non-capital loss available for carryforward to reduce future years' income for Canadian income tax purposes. The loss was incurred in 1992 and will expire in 1999. In addition, the Company has accumulated scientific research and development expenses that are available for indefinite carryforward as discretionary deductions of $6,135,000 (1995 - $5,880,000). The Company also has available $670,000 (1995 - $720,000) of net capital losses for an indefinite carryforward period to be applied against future capital gains. The tax effect has not been recorded in the financial statements. In 1996, the Company applied $2,320,000 (1995 - $1,052,000) of the losses carried forward to extinguish the income tax liability.

Also, the Company has investment tax credits available to reduce taxes payable of $1,963,000. The investment tax credits expire as follows:

1997	$ 7,000
1998	110,000
1999	260,000
2000	393,000
2001	297,000
2002	382,000
2003	193,000
2004	147,000
2005	98,000
2006	76,000
	$ 1,963,000

12. Other information:

(i) Geographic segments:

1996	Canada and Other	United States	Consolidated
Sales to external customers	$ 45,131,165	$ 12,362,456	$ 57,493,621
Earnings before interest costs and other items	$ 2,064,100	$ (192,964)	$ 1,871,136
Identifiable assets	$ 25,265,429	$ 5,330,162	$ 30,595,591

1995	Canada and Other	United States	Consolidated
Sales to external customers	$ 36,846,546	$ 11,926,837	$ 48,773,383
Earnings before interest costs and other items	$ 1,441,590	$ (536,313)	$ 905,277
Identifiable assets	$ 22,575,115	$ 4,758,235	$ 27,333,350

12. Other information (continued)

(ii) Export sales:

Revenue includes sales from the Canadian operations of the Company to geographic areas outside Canada for the fiscal years as follows:

	United States	United Kingdom & other countries
Fiscal 1996	$ 15,500,000	$ 1,700,000
Fiscal 1995	11,500,000	1,300,000

13. Commitments:

Future minimum payments under various operating lease agreements by fiscal year at December 31, 1996 are approximately as follows:

1997	$ 652,173
1998	623,585
1999	477,728
2000	179,687
	$ 1,933,173

14. Related party transactions:

The following table summarizes the Company's related party transactions for the year:

	1996	1995
Revenue:		
Sales of product to Cyberion	$ 70,000	$ —
Management fees to Cyberion	136,000	105,000

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

At the end of the year, the amounts due from related parties are as follows:

	1996	1995
Cyberion	$ 21,000	$ 101,000

The amounts due from the significantly influenced investee are due on demand and have arisen from the sales of services referred to above.

15. Financial instruments:

(a) Fair value:

For certain of the Company's financial instruments, including cash and cash equivalents, marketable securities, accounts receivable, bank indebtedness and accounts payable and accrued liabilities, the carrying amounts approximate fair value due to their immediate or short-term maturity.

The fair values of obligation under long-term debt, calculated at the present value of future contractual payments of principal and interest, discounted at the current market rates of interest available to the Company for debt instruments with similar terms and maturity, approximate their carrying values and, therefore, no additional disclosure is necessary.

(b) Concentration of credit risk:

The Company revenues are dependent on customers in the satellite communication and home entertainment industries. As these customers are geographically dispersed, concentration of credit risk is considered to be minimal.

16. Prior period adjustment:

As a result of an arbitration process through the International Chamber of Commerce, in July 1996, the Company and Teleport Europe GmbH ("Teleport Europe") came to an agreement regarding claims made against the Company for non-compliances with specifications in a product sales contract in 1993.

In exchange for the termination of legal proceedings by Teleport Europe, the Company agreed to deliver to Teleport Europe, free of charge, 500 satellite receiver units. In addition, Teleport Europe may acquire additional units at agreed upon prices per unit. The Company also committed to repair the satellite receivers delivered under the 1993 product sales contract, to a maximum of 200 units, at an agreed upon price per unit. All arbitration costs have been shared equally by both parties.

As a result of this agreement, costs of approximately $470,000 associated with this claim, including legal fees, arbitration costs and the costs of producing and delivering the 500 units have been recorded as a prior period adjustment to reflect the costs and liabilities associated with the sales contracts in 1993.

17. Contingency:

A claim has been made against the Company and certain other parties totalling $55 million plus interest and legal costs for damages alleged to have resulted from the distribution and sale of digital satellite receiving/decoding systems in Canada, in alleged contravention of certain statutory provisions and rights, certain contractual rights and certain copyrights. Management does not believe the Company has any obligation in respect of this claim. An initial hearing on the merits of this claim is set for June, 1997. As the likelihood of loss is not determinable and the amount of any potential loss is not reasonably estimable, no contingent liability has been recorded by the Company in respect of this claim.

Five Year Financial Summary

NII Norsat International Inc.

	1996	1995*	1994*	1993*	1992
Operating results ($000)					
Sales	**57,494**	48,773	37,250	18,649	16,788
Earnings (loss) before interest, taxes, depreciation and amortization	**2,738**	1,713	1,691	298	(3,027)
Net earnings (loss)	**2,069**	903	818	(361)	(8,094)
Balance sheet ($000)					
Working capital (deficiency)	**15,651**	14,406	8,893	6,844	(1,673)
Capital assets – net	**2,424**	2,415	2,360	2,157	2,443
Total assets	**30,596**	27,333	17,957	13,359	8,131
Long-term debt (excluding current portion)	**81**	84	3,021	3,293	2,003
Shareholders' equity (deficiency)	**21,160**	20,161	9,948	6,147	(1,297)
Changes in financial position ($000)					
Cash generated by (used in) operations (before changes in non-cash operating working capital)	**3,005**	1,757	1,503	344	(6,903)
Capital asset expenditures	**572**	558	514	347	488
Acquisitions of businesses	**—**	1,655	2,321	667	—
Equity issued	**20**	9,310	2,982	2,794	149
Per share ($)					
Net earnings (loss) – basic	**0.11**	0.05	0.06	(0.05)	(1.16)
Cash generated by operations	**0.15**	0.10	0.11	0.04	(0.99)
Book value	**1.07**	1.02	0.66	0.61	(0.19)
TSE/NASDAQ share price - High	**4.00**	6.00	2.34	2.27	3.20
- Low	**1.80**	1.40	1.35	0.82	0.73
Financial ratios					
Current ratio	**2.67**	3.03	2.78	2.75	0.77
Inventory turnover (average)	**5.45**	5.88	5.46	3.89	2.95
Debt/equity	**0.45**	0.36	0.81	1.17	N/A
Net earnings (loss)/sales (%)	**4%**	2%	2%	(2%)	(48%)
Return on equity (%)	**10%**	6%	9%	N/A	N/A
Additional information					
R&D expenditures ($000)	**343**	347	533	656	1,819
Sales per employee ($000)	**423**	397	388	214	149
Shares outstanding (000)	**19,753**	19,736	15,022	10,140	6,984
Number of employees (average)	**136**	123	96	87	113

* *restated for prior period adjustment*

Directors

Bruce H. Chapman
President & Chief Executive Officer

Ugo A. Doninelli
General Manager & Chief Executive Officer,
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President, Farragut Investments, Inc.

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Investor Relations

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Annual General Meeting

NII Norsat International Inc.'s annual general meeting will be held on Thursday, May 22 at the Hyatt Regency Vancouver, Grouse Room, at 2 p.m. (Pacific daylight time).

NII Norsat International Inc.

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